

Message Text

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ORIGIN EB-11

INFO OCT-01 AF-10 ISO-00 SS-20 SSO-00 NSCE-00 INRE-00

FEA-02 AEC-11 AID-20 CEA-02 CIAE-00 CIEP-02 COME-00

DODE-00 FPC-01 H-03 INR-11 INT-08 L-03 NSAE-00 NSC-07

OMB-01 PM-07 RSC-01 SAM-01 SCI-06 SP-03 STR-08

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DRAFTED BY EB/ORF/FSE:MCREEKMORE;AF/W:GMITCHELL

APPROVED BY D - RSING-RSOLL

AF:JJBLAKE

EB/ORF:JKATZ

AF/W:JLLOUGHRAN

S/S - SEFRY

EB/ORF/FSE:SBOSWORTH

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FM SECSTATE WASHDC

TO AMEMBASSY LAGOS IMMEDIATE

C O N F I D E N T I A L STATE 158884

E.O. 11652: GDS

TAGS- ENGR

SUBJECT: DEMARCHE ON HIGH OIL PRICES

FOR THE AMBASSADOR

1. ALTHOUGH OUR RELATIONS WITH OIL PRODUCING STATES ARE IMPROVING, FULL IMPLEMENTATION OF NEW COOPERATIVE RELATIONSHIPS WITH SOME PRODUCERS, WHICH ACCENTUATE COMPLEMENTARY INTERESTS AND REDUCE POINTS OF FRICTION, IS BEING INHIBITED BY CURRENT OPEC OIL PRICE POLICIES. IT IS OUR CONVICTION THAT WORLD OIL PRICES ARE MUCH TOO HIGH. THEY ARE STRAINING THE WORLD ECONOMY AND RETARDING ITS GROWTH. MAINTENANCE OF CURRENT PRICE LEVELS COULD CAUSE SERIOUS AND LAST-CONFIDENTIAL

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ING DISLOCATIONS AND LEAD TO VIRTUAL ECONOMIC COLLAPSE OF

SOME LDC'S. ON BASIS CURRENT MARKET CONDITIONS, WE BELIEVE OIL PRICES SHOULD BE FALLING RATHER THAN RISING- CONSEQUENTLY, WE CONSIDER RECENT OPEC DECISION TO RAISE ROYALTIES BY 2 PERCENT AS UNWARRANTED EVEN THOUGH THIS INCREASE WAS SMALL IN COMPARISON TO PRIOR INCREASES.

2. WE WISH TO EMPHASIZE TO THE PRODUCERS OUR VIEWS ON PRICES. HOWEVER, IN REMONSTRATING AGAINST THE HIGH PRICES, WE MUST AT THE SAME TIME TAKE INTO CONSIDERATION OUR OVERALL INTERESTS WITH PRODUCER STATES. BY STRESSING IN DEMARCHES WE MAKE TO PRODUCER GOVTS POSITIVE ELEMENTS IN ADDITION TO FOCUSING ON THORNY SUBJECTS SUCH AS PRICE,

WE AIM BOTH TO MODERATE PRODUCERS' DEMONSTRATED SENSITIVITIES ON THOSE SUBJECTS AND TO EMPHASIZE TOTALITY OF US-PRODUCER COUNTRY RELATIONS.

3. OUR EMBASSIES IN ALL OPEC COUNTRIES EXCEPT SAUDI ARABIA ARE BEING INSTRUCTED TO EXPRESS OUR OPPOSITION TO CURRENT HIGH PRICE LEVELS, AND TO INDICATE OUR CONVICTION THAT LOWER PRICES ARE IN THE LONG TERM INTEREST OF PRODUCERS AS WELL AS CONSUMERS. IN THOSE COUNTRIES THAT HAVE ANNOUNCED NEW PRICE INCREASES SINCE THE JUN OPEC MEETING, OUR AMBASSADORS HAVE POINTED OUT OUR BELIEF THAT THESE INCREASES WERE UNWARRANTED AND OUR HOPE THAT THESE PRICE DECISIONS WOULD BE RECONSIDERED.

4. YOU SHOULD SEEK AN EARLY OPPORTUNITY WITH APPROPRIATE SENIOR FMG OFFICIALS TO EMPHASIZE OUR VIEWS ON OIL PRICES AND TO ENCOURAGE THEM NOT TO RAISE PRICES FURTHER. IN MAKING YOUR REPRESENTATION, YOU SHOULD DRAW ON THE FOLLOWING POINTS:

--I HAVE BEEN INSTRUCTED TO BRING TO THE ATTENTION OF THE NIGERIAN GOVT, MY GOVT'S DEEP CONCERN WITH OIL PRICE DEVELOPMENTS. THIS CONCERN IS ALSO BEING EXPRESSED TO OTHER OPEC GOVTS AS WELL AS YOURS.

--THE UNITED STATES BELIEVES THAT WORLD OIL PRICES ARE ALREADY CRITICALLY HIGH. AS A RESULT, THE WORLD ECONOMY IS DANGEROUSLY STRAINED AND WORLD DEVELOPMENT IS BEING

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RETARDED. THE NEW INCREASES JUST ANNOUNCED BY SOME OPEC GOVTS WILL COMPOUND THE DIFFICULTIES CONSUMING COUNTRIES FACE IN TRYING TO ADJUST TO THE ENORMOUS AND ABRUPT INCREASE IN OIL PRICES OVER THE PAST 18 MONTHS. WE SINCERELY HOPE YOUR GOVT WILL NOT ADD TO THESE DIFFICULTIES BY FURTHER RAISING ITS PRICES.

--THE DIRECT AND INDIRECT BURDEN OF HIGH OIL PRICES

ON THE WORLD'S CONSUMERS IS A HEAVY ONE. THE PLIGHT OF DEVELOPING CONSUMER COUNTRIES IS PRESSING; IN SOME CASES, INCREASED EXPENDITURES FOR ENERGY ARE SURPASSING THEIR TOTAL AID RECEIPTS AND COULD LEAD TO VIRTUAL ECONOMIC COLLAPSE.

--WE BELIEVE CURRENT HIGH PRICE LEVELS ARE IN THE INTEREST OF NEITHER CONSUMERS NOR PRODUCERS. IN THE SHORT RUN, THEY HURT CONSUMERS. BUT IN THE LONG RUN, PRODUCERS WILL ALSO LOSE BECAUSE MAINTENANCE OF HIGH PRICES WILL STIMULATE EVEN GREATER RESEARCH AND INVESTMENT INTO ALTERNATIVE SOURCES OF ENERGY AND ALTERNATIVES TO ENERGY USE. THE EFFECT WILL BE TO REDUCE THE TOTAL VALUE THE OIL EXPORTERS RECEIVE OVER THE LIFE OF THEIR PRODUCING FIELDS.

THE NET RESULT WILL BE DISADVANTAGEOUS TO ALL.

--WE RECOGNIZE THAT PRODUCING COUNTRIES ARE ANXIOUS TO PROTECT THEIR REAL EARNINGS IN THE CURRENT WORLD-WIDE INFLATION. HOWEVER, THESE COUNTRIES SHOULD ALSO RECOGNIZE THAT THE TREMENDOUS INCREASES IN OIL PRICES OF THE PAST SEVERAL MONTHS ARE IN THEMSELVES A MAJOR CAUSE OF WORLD INFLATION. THUS, EFFORTS TO OFFSET INFLATION BY RAISING PRICES ARE NOT ONLY SHORTSIGHTED BUT ALSO COUNTER-PRODUCTIVE.

--IN OUR INTERDEPENDENT WORLD, THE ECONOMIC FUTURES OF ALL COUNTRIES ARE CLOSELY RELATED. ALL NATIONS, PRODUCERS AND CONSUMERS, WILL SUFFER IN A WORLD THAT IS CHARACTERIZED BY FALTERING AND FAILING ECONOMIES. WE URGE YOUR GOVT TO RECONSIDER ITS PRICING POLICY IN GENERAL. IN PARTICULAR, WE HOPE YOU WILL NOT INCREASE PRICES FURTHER AT THIS TIME.

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--A RESOLUTION OF DIFFERING VIEWS ON PRICING IS URGENT AND ESSENTIAL. HOWEVER, AS BOTH SIDES NOW BEGIN TO WORK OUT THIS DIFFICULT BUT NOT INSOLUBLE PROBLEM, WE BELIEVE IT IS IN THE INTEREST OF PRODUCERS AND CONSUMERS NOT TO LOSE THEMSELVES IN POLEMICS. THIS COULD INHIBIT GROWING AND BENEFICIAL TRENDS TOWARDS COMPLEMENTARY FINANCIAL, COMMERCIAL, AND INDUSTRIAL PROGRAMS WHICH HOLD SO MUCH PROMISE FOR ALL CONCERNED, BUT WHICH MUST BE BASED UPON A STABLE SUPPLY OF ENERGY TO THE GLOBAL ECONOMY.

--TO THIS END, AND IN REALIZATION THAT STABLE SUPPLY AT REASONABLE PRICES IS CRUCIAL TO ANY CONSIDERATION OF ENERGY PROBLEMS, WE HOPE TO ENCOURAGE A DIALOGUE WITH PRODUCER STATES WHICH DOES NOT FOCUS ON OIL PRICES TO THE EX-

CLUSION OF THE MANY OTHER VERY IMPORTANT ASPECTS OF PRODUCER/CONSUMER RELATIONS.

5. IN REPLY, LOCAL GOVT OFFICIALS MAY SAY THAT INCREASED OIL PRICES ARE JUSTIFIED TO OFFSET THE HIGHER PRICES THE OIL EXPORTING STATES MUST PAY FOR IMPORTS FROM THE INDUSTRIALIZED COUNTRIES. THEY MAY CONTEND THAT THEIR COUNTRIES ARE PAYING TWO-THREE TIMES MORE FOR WHEAT AND TWICE AS MUCH FOR STEEL PRODUCTS THAN IN 1972. THEY SHOULD BE REMINDED, HOWEVER, THAT OIL PRICE INCREASES WERE NOT ONLY LARGER BUT MORE ABRUPT AND THEREFORE MORE DISRUPTIVE THAN FOR THOSE OF ANY OTHER COMMODITY. FURTHERMORE, THE US HAS MOVED VIGOROUSLY TO COUNTER HIGH PRICES ON ITS OWN AGRICULTURAL EXPORTS BY EXPANDING ACREAGE AND INCREASING PRODUCTION. AS A CONSEQUENCE, WHEAT PRICES HAVE FALLEN SUBSTANTIALLY FROM EARLIER HIGHS. THE US STEEL INDUSTRY IS

CURRENTLY PRODUCING AT FULL CAPACITY.

6. YOU WILL ALSO PROBABLY BE TOLD THAT THE OPEC DECISION TO RAISE ROYALTY OR OTHER TAXES IS DESIGNED TO REDUCE COMPANIES' "EXCESS PROFITS" AND NOT RAISE THE COST TO THE CONSUMER. IN FACT, ANY SUCH INCREASE WILL BE PASSED ON. WHEN THE OPEC TECHNICIANS TALK OF EXCESS PROFITS THEY APPEAR TO ASSUME THAT THE COMPANIES SELL THEIR EQUITY OIL, WHICH COSTS ON THE AVERAGE SLIGHTLY MORE THAN \$7 A BARREL, CONFIDENTIAL

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AT 93 PERCENT OF POSTED PRICE (IN EXCESS OF \$10.40). WHAT ACTUALLY HAPPENS IS THAT COMPANIES AVERAGE THE COSTS OF THEIR EQUITY AND PARTICIPATION CRUDES IN DETERMINING THEIR TRANSFER PRICES. AN INCREASE IN ROYALTY OR OTHER TAXES WOULD CONSEQUENTLY BE REFLECTED IN A HIGHER AVERAGE PER BARREL COST TO THE COMPANY AND IN A HIGHER PRICE TO THE CONSUMER. WITH REGARD TO THE VERY LARGE PROFITS REPORTED BY THE COMPANIES IN THE LAST QUARTER OF 1973 AND FIRST QUARTER OF 1974, THE COMPANIES POINT TO THE SPECIAL ONE-TIME EFFECTS OF FOREIGN EXCHANGE GAINS AND PROFITS REALIZED FROM REVALUING LOW COST INVENTORIES.

7. FYI: IN VIEW OF ADAMANT POSITION TAKEN BY MOST OPEC MEMBERS IN FAVOR OF INCREASED OIL PRICES, WE DO NOT EXPECT HOST GOVT TO RESPOND TO YOUR DEMARCHE BY IMMEDIATELY MODIFYING POLICY. HOWEVER, WE BELIEVE IT IS IMPORTANT FOR THEM TO UNDERSTAND CLEARLY THE VIEWPOINT OF THE USG, TO REALIZE THAT WE ARE SERIOUSLY CONCERNED ABOUT THE WORLD-WIDE ECONOMIC DISLOCATION WHICH HAS RESULTED FROM OIL PRICING POLICIES, AND TO BE INFORMED THAT WE DO NOT BELIEVE FURTHER PRICE INCREASES CAN BE JUSTIFIED UNDER THE PRESENT CONDITIONS.

8. PLEASE REPORT THE REACTION OF YOUR HOST GOVT TO OUR
DEMARCHE. KISSINGER

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NNN

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